Notes on -SEBI Regulations on Mutual Funds And AMFI

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SEBI regulations on mutual funds

Important steps taken by SEBI for the regulation of mutual funds are listed below:

(1) Formation:

Certain structural changes have also been made in the mutual fund industry, as part of which mutual funds are required to set up asset management companies with fifty percent independent directors, separate board of trustee companies, consisting of a minimum fifty percent of independent trustees and to appoint independent custodians.

This is to ensure an arm's length relationship between trustees, fund managers and custodians, and is in contrast with the situation prevailing earlier in which all three functions were often performed by one body which was usually the sponsor of the fund or a subsidiary of the sponsor.

Thus, the process of forming and floating mutual funds has been made a tripartite exercise by authorities. The trustees, the asset management companies (AMCs) and the mutual fund shareholders form the three legs. SEBI guidelines provide for the trustees to maintain an arm's length relationship with the AMCs and do all those things that would secure the right of investors.

With funds being managed by AMCs and custody of assets remaining with trustees, an element of counter-balancing of risks exists as both can keep tabs on each other.

(2) Registration:

In January 1993, SEBI prescribed registration of mutual funds taking into account track record of a sponsor, integrity in business transactions and financial soundness while granting permission.

This will curb excessive growth of the mutual funds and protect investor's interest by registering only the sound promoters with a proven track record and financial strength. In February 1993, SEBI cleared six private sector mutual funds viz. 20th Century Finance Corporation, Industrial Credit & Investment Corporation of India, Tata Sons, Credit Capital Finance Corporation, Ceat Financial Services and Apple Industries.

(3) Documents:

The offer documents of schemes launched by mutual funds and the scheme particulars are required to be vetted by SEBI. A standard format for mutual fund prospectuses is being formulated.

(4) Code of advertisement:

Mutual funds have been required to adhere to a code of advertisement.

(5) Assurance on returns:

SEBI has introduced a change in the Securities Control and Regulations Act governing the mutual funds. Now the mutual funds were prevented from giving any assurance on the land of returns they would be providing. However, under pressure from the mutual funds, SEBI revised the guidelines allowing assurances on return subject to certain conditions.

Hence, only those mutual funds which have been in the market for at least five years are allowed to assure a maximum return of 12 per cent only, for one year. With this, SEBI, by default, allowed public sector mutual funds an advantage against the newly set up private mutual funds.

As per basic tenets of investment, it can be justifiably argued that investments in the capital market carried a certain amount of risk, and any investor investing in the markets with an aim of making profit from capital appreciation, or otherwise, should also be prepared to bear the risks of loss.

(6) Minimum corpus:

The current SEBI guidelines on mutual funds prescribe a minimum start-up corpus of Rs.50 crore for a open-ended scheme, and Rs.20 crore corpus for closed-ended scheme, failing which application money has to be refunded.

The idea behind forwarding such a proposal to SEBI is that in the past, the minimum corpus requirements have forced AMCs to solicit funds from corporate bodies, thus reducing mutual funds into quasi-portfolio management outfits. In fact, the Association of Mutual Funds in India (AMFI) has repeatedly appealed to the regulatory authorities for scrapping the minimum corpus requirements.

(7) Institutionalisation:

The efforts of SEBI have, in the last few years, been to institutionalise the market by introducing proportionate allotment and increasing the minimum deposit amount to Rs.5000 etc. These efforts are to channel the investment of individual investors into the mutual funds.

(8) Investment of funds mobilised:

In November 1992, SEBI increased the time limit from six months to nine months within which the mutual funds have to invest resources raised from the latest tax saving schemes. The guideline was issued to protect the mutual funds from the disadvantage of investing funds in the bullish market at very high prices and suffering from poor NAV thereafter.

(9) Investment in money market:

SEBI guidelines say that mutual funds can invest a maximum of 25 per cent of resources mobilised into money-market instruments in the first six months after closing the funds and a maximum of 15 per cent of the corpus after six months to meet short term liquidity requirements.

Private sector mutual funds, for the first time, were allowed to invest in the call money market after this year's budget. However, as SEBI regulations limit their exposure to money markets, mutual funds are not major players in the call money market. Thus, mutual funds do not have a significant impact on the call money market.

(10) Valuation of investment:

The transparent and well understood declaration or Net Asset Values (NAVs) of mutual fund schemes is an important issue in providing investors with information as to the performance of the fund. SEBI has warned some mutual funds earlier of unhealthy market

(11) Inspection:

SEBI inspect mutual funds every year. A full SEBI inspection of all the 27 mutual funds was proposed to be done by the March 1996 to streamline their operations and protect the investor's interests. Mutual funds are monitored and inspected by SEBI to ensure compliance with the regulations.

(12) Underwriting:

In July 1994, SEBI permitted mutual funds to take up underwriting of primary issues as a part of their investment activity. This step may assist the mutual funds in diversifying their business.

(13) Conduct:

In September 1994, it was clarified by SEBI that mutual funds shall not offer buy back schemes or assured returns to corporate investors. The Regulations governing Mutual Funds and Portfolio Managers ensure transparency in their functioning.

(14) Voting rights:

In September 1993, mutual funds were allowed to exercise their voting rights. Department of Company Affairs has reportedly granted mutual funds the right to vote as full-fledged shareholders in companies where they have equity investments.

AMFI

The Association of Mutual Funds in India is an industry standards organisation in India in the mutual funds sector. It was formed in 1995. Most mutual funds firms in India are its members. The organisation aims to develop the mutual funds market in India, by improving ethical and professional standards. **The Association of Mutual Funds in India** (AMFI) is dedicated to developing the Indian Mutual Fund Industry on professional, healthy and ethical lines and to enhance and maintain standards in all areas with a view to protecting and promoting the interests of mutual funds and their unit holders.

AMFI, the association of all the Asset Management Companies of SEBI registered mutual funds in India, was incorporated on August 22, 1995, as a non-profit organisation. As of now, all the 45 Asset Management Companies that are registered with SEBI, are its members.

OBJECTIVES

- To define and maintain high professional and ethical standards in all areas of operation of mutual fund industry.
- To recommend and promote best business practices and code of conduct to be followed by members and others engaged in the activities of mutual fund and asset management including agencies connected or involved in the field of capital markets and financial services.
- To interact with the Securities and Exchange Board of India (SEBI) and to represent to SEBI on all matters concerning the mutual fund industry.
- To represent to the Government, Reserve Bank of India and other bodies on all matters relating to the Mutual Fund Industry.
- To undertake nation wide investor awareness programme so as to promote proper understanding of the concept and working of mutual funds.
- To disseminate information on Mutual Fund Industry and to undertake studies and research directly and/or in association with other bodies.
- To take regulate conduct of distributors including disciplinary actions (cancellation of ARN) for violations of Code of Conduct.
- To protect the interest of investors/unit holders.